

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

Number: **200924008**

Release Date: 6/12/2009

Index Number: 61.00-00, 1001.00-00,
2501.00-00, 2601.00-00;

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:PSI:B04 – PLR-137971-08

Date:

February 12, 2009

Legend:

Settlor	=
Spouse	=
Child 1	=
Child 2	=
Child 3	=
Grandchild 1	=
Grandchild 2	=
Grandchild 3	=
Grandchild 4	=
Grandchild 5	=
Date 1	=
Trust	=
State	=
State Court	=
State Law 1	=
State Law 2	=
<u>X</u>	=

Dear _____ :

This letter responds to a letter dated July 17, 2008, from your authorized representative, requesting rulings under §§ 2501 and 2601 of the Internal Revenue Code with respect to a proposed distribution of principal from five trusts to five new trusts and modifications to the original trust instrument.

On Date 1, Settlor established Trust for the benefit of Settlor's issue. Settlor and his spouse, Spouse, are deceased. Settlor's surviving issue include: Child 1 and her two children, Grandchild 1 and 2; Child 2 and her three children, Grandchild 3-5, and Child 3, who has no children.

Under Article First of Trust, during the lifetime of the survivor of Child 1 and 2, the trustees are to divide the net income into one share for each of the surviving issue of Child 1, Child 2, and Child 3, and if a child of Settlor does not have any surviving issue, then one share for the child. The trustees have the discretion, at any time and from time to time during Trust, to pay all or any part of the trust principal to the income beneficiary of each share, provided however, that the beneficiary receives the same percentage of principal as the percentage to which he or she is entitled to receive from the current income of his or her share.

Under Article First, upon the death of the survivor of Child 1 or 2, Trust is to terminate and the trustees will distribute the principal to the surviving issue of all of Settlor's children in equal shares per stirpes, provided however, if any child of the Settlor is living and has no surviving issue, then that share will be paid to the child. If Settlor's issue are deceased at the time of termination of Trust, then the principal will be paid to the surviving issue of the Settlor's brother and sisters in equal shares per stirpes.

Under Article Tenth, the trustees, in their discretion, may from time to time set up separate trusts for each of the beneficiaries provided that each beneficiary will receive his or her pro rata share of Trust.

Pursuant to Article Tenth, Trust was divided into six separate trusts (Separate Trusts), one trust for each grandchild (Grandchild 1-5) and one trust for Child 3. The division was based on each beneficiary's applicable share of the current income of Trust. Each Separate Trust and Trust are identical except that the trustees of each Separate Trust are required to pay income and principal, in their discretion, from a Separate Trust to the sole beneficiary of that Separate Trust. The trustees of the Separate Trusts for Grandchild 1 and Grandchild 2 are Child 1, Child 2, and X. The trustees of the Separate Trust for Grandchild 3 are Child 2, Grandchild 3, and X. The trustees of the Separate Trust for Grandchild 4 are Child 2, Grandchild 4, and X. The trustees of the Separate Trust for Grandchild 5 are Child 2, Grandchild 5, and X. The trustees for the Separate Trust of Child 3 are Child 2, Child 3, and X. Trust and the Separate Trusts are subject to the laws of State.

Subject to the receipt of a favorable private letter ruling, the trustees of the Separate Trusts will petition State Court for an order approving the trustees' distribution of principal from each Separate Trust to six new trusts (Further Trusts), one trust to benefit each Grandchild and one trust to benefit Child 3. The terms of each Further Trust will be identical to the terms of the Separate Trusts, except that each Further Trust will terminate on the death of the sole beneficiary of that trust and each beneficiary will have a testamentary general power to appoint the trust corpus of his or her Further Trust to anyone, including his or her estate.

Trust became irrevocable prior to September 25, 1985, and it is represented that no additions have been made to Trust or the Separate Trusts after Date 1, the date Trust was established and funded.

You have requested the following rulings:

1. The distribution of principal from the Separate Trusts to the Further Trusts and the modifications of the original trust instrument, as approved by State Court, will not affect the GST exempt status of the Further Trusts.
2. The proposed transaction will not result in any gift for federal gift tax purposes by Grandchild 1-5.

Ruling Request 1

Section 2601 imposes a tax on every generation-skipping transfer (GST), which is defined under § 2611 as a taxable distribution, a taxable termination, or a direct skip.

Under section 1433 of the Tax Reform Act of 1986 (the Act), the GST tax is generally applicable to generation-skipping transfers made after October 22, 1986. However, under § 1433(b)(2)(A) of the Act and § 26.2601-1(b)(1)(i) of the Generation-Skipping Transfer Tax Regulations, the tax does not apply to a transfer under a trust that was irrevocable on September 25, 1985, except to the extent the transfer is made out of corpus added to the trust by an actual or constructive addition after September 25, 1985.

Section 26.2601-1(b)(4)(i) provides rules for determining when a modification, judicial construction, settlement agreement, or trustee action with respect to a trust that is exempt from the generation-skipping transfer tax under § 26.2601-1(b) will not cause the trust to lose its exempt status. These rules are applicable only for purposes of determining whether an exempt trust retains its exempt status for generation-skipping transfer tax purposes. The rules do not apply in determining, for example, whether the transaction results in a gift subject to gift tax, or may cause the trust to be included in the gross estate of a beneficiary, or may result in the realization of capital gain for purposes of § 1001.

Section 26.2601-1(b)(4)(i)(A) provides that the distribution of trust principal from an exempt trust to a new trust or retention of trust principal in a continuing trust will not cause the new or continuing trust to be subject to the provisions of chapter 13, if –

(1) Either --

(i) The terms of the governing instrument of the exempt trust authorize distributions to the new trust or the retention of trust principal in a continuing trust, without the consent or approval of any beneficiary or court; or

(ii) at the time the exempt trust became irrevocable, state law authorized distributions to the new trust or retention of principal in the continuing trust, without the consent or approval of any beneficiary or court; and

(2) The terms of the governing instrument of the new or continuing trust do not extend the time for vesting of any beneficial interest in the trust in a manner that may postpone or suspend the vesting, absolute ownership, or power of alienation of an interest in property for a period, measured from the date the original trust became irrevocable, extending beyond any life in being at the date the original trust became irrevocable plus a period of 21 years, plus if necessary, a reasonable period of gestation.

Section 26.2601-1(b)(4)(i)(D) provides that a modification of the governing instrument of an exempt trust by judicial reformation, or nonjudicial reformation that is valid under applicable state law, will not cause an exempt trust to be subject to the provisions of chapter 13 if the modification does not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation (as defined in § 2651) than the person or persons who held the beneficial interest prior to the modification, and the modification does not extend the time for vesting of any beneficial interest in the trust beyond the period provided for in the original trust. A modification of an exempt trust will result in a shift in a beneficial interest to a lower generation beneficiary if the modification can result in either an increase in the amount of a generation-skipping transfer or the creation of a new generation-skipping transfer.

Section 26.2601-1(b)(4)(i)(E), Example 1, considers a situation where, in 1980, Grantor established an irrevocable trust (Trust) for the benefit of Grantor's child, A, A's spouse, and A's issue. At the time Trust was established, A had two children, B and C. A corporate fiduciary was designated as trustee. Under the terms of Trust, the trustee has the discretion to distribute all or part of the trust income to one or more of the group consisting of A, A's spouse or A's issue. The trustee is also authorized to distribute all or part of the trust principal to one or more trusts for the benefit of A, A's spouse, or A's issue under terms specified by the trustee in the trustee's discretion. Any trust established under Trust, however, must terminate 21 years after the death of the last child of A to die who was alive at the time Trust was executed. Trust will terminate on the death of A, at which time the remaining trust principal will be distributed to A's issue, per stirpes. In 2002, the trustee distributes part of Trust's principal to a new trust for the benefit of B and C and their issue. The new trust will terminate 21 years after the death of the survivor of B and C, at which time the trust principal will be distributed to the issue of B and C, per stirpes. The terms of the governing instrument of Trust authorize the trustee to make the distribution to a new trust without the consent or approval of any beneficiary or court. In addition, the terms of the governing instrument of the new trust do not extend the time for vesting of any beneficial interest in a manner that may postpone or suspend the vesting, absolute ownership or power of alienation of an interest in property for a period, measured from the date of creation of Trust, extending beyond any life in being at the date of creation of Trust plus a period of 21 years, plus if necessary, a reasonable period of gestation. Therefore, neither Trust nor the new trust will be subject to the provisions of chapter 13.

State Law 1 provides that a trustee who has the absolute discretion, under the terms of a testamentary instrument or an irrevocable inter vivos trust agreement, to invade the principal of a trust for the benefit of one or more proper objects of the exercise of the power, may exercise this discretion by appointing all or part of the principal of the trust in

another trust, under a different instrument, for the benefit of the proper objects of the exercise of that power. Under State Law 2, a trustee may exercise the powers granted by State Law 1 without the consent of any interested person and without seeking court approval or, alternatively, a trustee may seek court approval of the exercise of its authority under State Law. Under State Law 2, upon a petition of the trustee, and upon notice to all persons interested in the trust, the court having jurisdiction over the trust may direct the trustee to exercise its discretion under State Law by appointing all or part of the principal of the trust in favor of a trustee of a trust under an instrument other than that under which the power to invade is created or under the same instrument.

In the instant case, the distribution of principal from each Separate Trust to each Further Trust is pursuant to the terms of the governing instrument of Trust which authorizes distributions of principal to new trusts without the consent or approval of any beneficiary or court. Pursuant to the modifications of Trust, each beneficiary of each Further Trust will possess a general power of appointment. Accordingly, the terms of each Further Trust will not extend the time for vesting of any beneficial interest in the trust in a manner that may postpone or suspend the vesting, absolute ownership, or power of alienation of an interest in property for a period, measured from the date the original trust became irrevocable, extending beyond any life in being at the date the original trust became irrevocable plus a period of 21 years, plus if necessary, a reasonable period of gestation.

Further, the proposed modifications to each Further Trust will not shift a beneficial interest in the trust to any beneficiary who occupies a lower generation (as defined in § 2651) than the person or persons who held the beneficial interest prior to the modification. Therefore, based on the facts submitted and representations made, we conclude that the distribution of principal from each Separate Trust to each Further Trust and the modifications to Trust, as approved by State Court, will not cause the Further Trusts to lose their exempt status for generation-skipping transfer tax purposes under § 2601.

Ruling Request 2

Section 2501 imposes a tax on the transfer of property by gift by any individual.

Section 2511(a) provides that the gift tax applies whether the transfer is in trust or otherwise, whether the gift is direct or indirect, and whether the property is real or personal, tangible or intangible.

Section 25.2511-1(c)(1) of the Gift Tax Regulations provides that the gift tax also applies to gifts indirectly made. Thus, any transaction in which an interest in property is gratuitously passed or conferred upon another, regardless of the means or device employed, constitutes a gift subject to tax.

In this case, the beneficial interests in each Further Trust will be identical to the beneficial interests in each Separate Trust. Therefore, no interest in the Separate Trusts will be passed gratuitously to the Further Trusts. Accordingly, based upon the facts submitted and representations made, we conclude that the distribution of principal of each

Separate Trust to the Further Trusts and the modifications to Trust will not be subject to gift tax under § 2501.

Except as specifically ruled herein, we express no opinion on the federal tax consequences of the facts described above under the cited provisions or any other provisions of the Code or regulations.

The rulings contained in this letter are based upon information and representations submitted by the taxpayers and accompanied by penalty of perjury statements executed by the appropriate parties. While this office has not verified any part of the material submitted in support of the request for rulings, it is subject to verification and examination.

This ruling is directed only to the taxpayers who requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Pursuant to the power of attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

Lorraine E. Gardner
Senior Counsel, Branch 4
(Passthroughs and Special Industries)

Enclosure

Copy for § 6110 purposes
Copy of this letter